REPORT OF EXAMINATION
OF THE

INTERINSURANCE EXCHANGE OF
THE AUTOMOBILE CLUB

AS OF
DECEMBER 31, 2003

Participating State
and Zone:

California

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Los Angeles, California
October 15, 2004

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition (EX4) Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable John Morrison
Secretary, Zone IV-Western
Commissioner of Insurance and Securities
Montana Department of Insurance Company
Helena, Montana

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman and Commissioners:

Pursuant to your instructions, an examination was made of the

INTERINSURANCE EXCHANGE OF THE AUTOMOBILE CLUB

(hereinafter also referred to as the Company) at the primary location of its books and records, 3333 Fairview Road, Costa Mesa, California 92626. The Company's statutory home office is located at 2601 South Figueroa Street, Los Angeles, California 90007.

SCOPE OF EXAMINATION

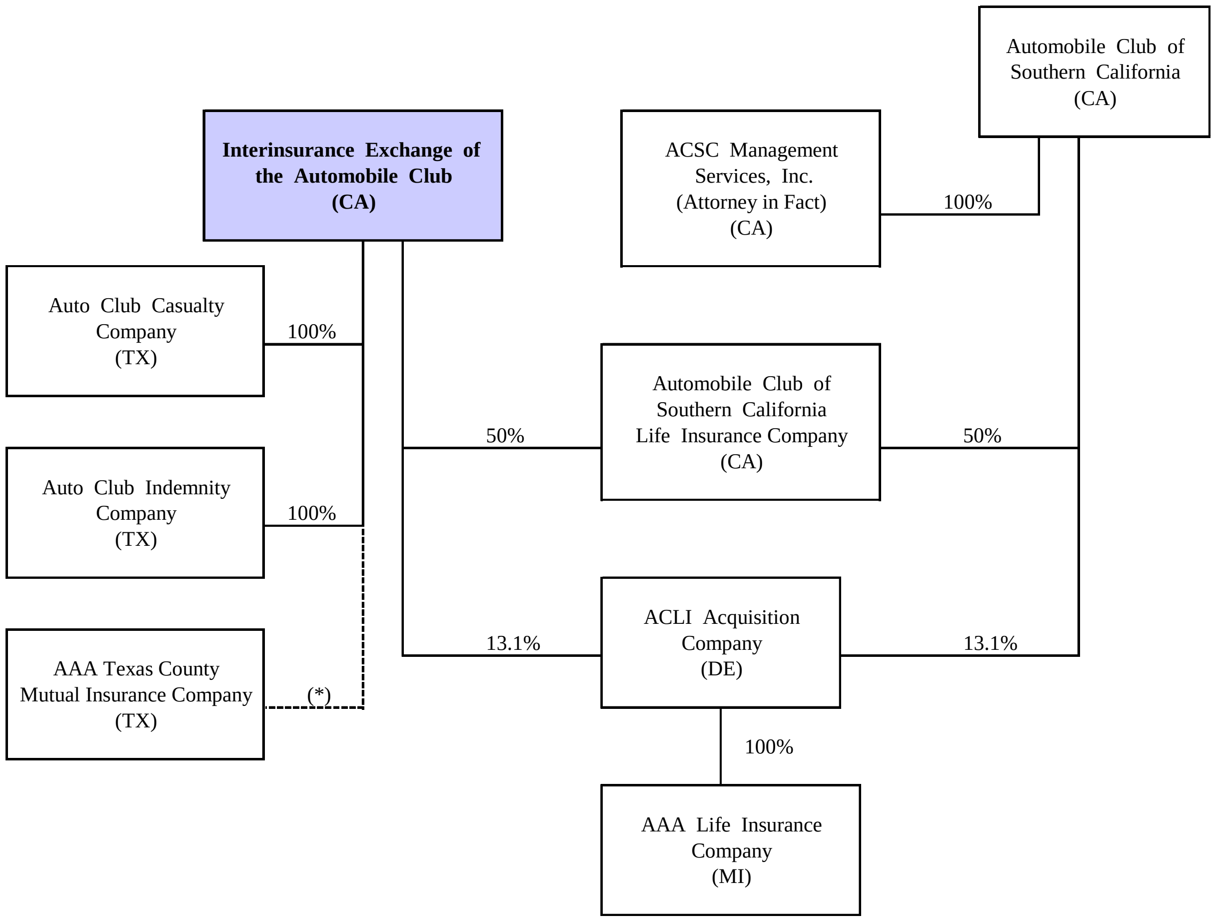
The previous examination of the Company was made as of December 31, 2000. This examination covers the period from January 1, 2001 through December 31, 2003. The examination was made pursuant to the National Association of Insurance Commissioners' (NAIC) plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2003, as deemed necessary under the circumstances.

This examination was conducted concurrently with the examination of the Automobile Club of Southern California Life Insurance Company (ACSC Life). The Company and the Automobile Club of Southern California each have a 50% ownership interest in ACSC Life.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed, including the following areas that require no further comment: company history; corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; accounts and records; and sales and advertising.

MANAGEMENT AND CONTROL

The following abridged organizational chart depicts the Company's relationship within the holding company system:



(*) Contractual relationship to operate the Company

Management of the Company is vested in a six-member board of governors. A listing of the members of the board and principal officers of the Company's Attorney-in-Fact serving on December 31, 2003 follows:

Board of Governors

Name and Residence	Principal Business Affiliation
Willis B. Wood, Jr. Fullerton, California	Retired Chairman, Chief Executive Officer and President Pacific Enterprises
Susan Corrales-Diaz Orange, California	President Systems Integrated
Byron E. Allumbaugh Newport Beach, California	Retired Chairman and Chief Executive Officer Ralphs Grocery Company
David R. Carpenter Santa Barbara, California	Chairman and Chief Executive Officer UniHealth Foundation
Edward M. Carson Beverly Hills, California	Retired Chairman and Chief Executive Officer First Interstate Bancorp
Gilbert T. Ray Los Angeles, California	Retired Partner O'Melveny & Meyers, LLP

Principal Officers of the Company's Attorney-in-Fact

Name	Title
Thomas V. McKernan, Jr.	President and Chief Executive Officer
Henry R. Toofanian	Secretary
John F. Boyle	Senior Vice President, Chief Financial Officer and Treasurer
Robert T. Bouttier	Senior Vice President, Marketing, Product and Member Services

Name	Title
Avery R. Brown	Vice President, Assistant Secretary and General Counsel
James Gilmartin	Senior Vice President, Insurance Operations
Stephen E. Lenzi	Senior Vice President, Public Affairs and Legal
Sharon B. Neiman	Senior Vice President, Insurance Sales and Services

Management Agreements

Management Agreement: Pursuant to a management agreement effective December 19, 1996, the Company's attorney-in-fact, ACSC Management Services, Inc. (ACSC Management) performs all of the operations of the Company. ACSC Management provides services related to the acquisition and issuance of insurance and the administrative activities associated with the business of the Company. In consideration for services rendered, the Company pays ACSC Management the following:

(1) A sum equal to 1% of the premiums earned less the tax computed according to the provisions of California Insurance Code Section 1530; and
(2) A sum equal to the amount of the operating expenses incurred (i.e. cost reimbursement) by ACSC Management for the performance of the above-indicated services.

Under the terms of the agreement the following fees were paid: $249,017,818 in 2001; $300,436,875 in 2002; and $324,522,460 in 2003. This agreement has been filed with the California Department of Insurance (CDI).

Investment Management Agreements: The Company has numerous investment management agreements with several non-affiliated entities, including but not limited to the following: Banc of America Capital Management; Delta Asset Management; Neuberger Berman, LLC; Nicholas Applegate Capital Management; State Street Global Advisors; Banc One Investment Advisors Corporation; BlackRock Financial Management; Citigroup Asset Management; Denver Investment

Advisors, LLC; Loomis Sayles & Company, LP; Oaktree Capital Management, LLC; Standish Mellon Asset Company; STW Fixed Income Management; T. Rowe Price; and Wellington Management Company, LLP. Under the investment agreements, these entities act as the Company's investment advisors in relation to cash, cash equivalents, fixed income securities or equities. The investment or reinvestment of the Company's securities is administered pursuant to the Company's investment guidelines. During the examination period the Company paid the following investment related fees: $4,738,490 in 2001, $4,470,783 in 2002, and $5,053,513 in 2003.

Tax Sharing Agreement: On February 2, 2000, the Company entered into a Tax Sharing Agreement with its subsidiaries, Auto Club Indemnity Company and Auto Club Casualty Company. Under the terms of the agreement, allocation of taxes is based upon separate return calculations and all settlement of inter-company tax balances are made within 30 days after the filing. This agreement was submitted and approved by the CDI.

On September 30, 2002, the Company purchased a management agreement from Countrywide Corporation for $7.2 million, to operate Industrial County Mutual Insurance Company (ICM). Upon the purchase of the management agreement, the name of ICM was changed to AAA Texas County Mutual Insurance Company (AAA TCM). Effective October 1, 2002, the Company entered into a quota share reinsurance agreement with AAA TCM to assume 100% of the business. This agreement was submitted and approved by the CDI.

Guaranty Agreement

Guaranty Agreement: On August 18, 1999, the Company, the Automobile Club of Southern California (Club), and the Automobile Club of Southern California Life Insurance Company (ACSC Life) entered into a Guaranty Agreement, whereby the Company and the Club unconditionally guaranteed the "solvency" of the ACSC Life. The Guaranty Agreement expired in December 2002 and was not renewed. In its place, the Company, the Club and ACSC Life entered into a commitment letter under which the Company and the Club each commit to pay 50% of the capital contributions to ACSC Life, in such amounts, as may be required in order for it to maintain a minimum risk-based capital ratio of 250%. The commitment letter has been reviewed and approved by the CDI. During the examination period, the Company and the Club made the following contributions to ACSC Life:

Year	**Contributions from the Company**	**Contributions from the Club**
2001	$ 500,000	$ 500,000
2002	$ 5,000,000	$ 5,000,000
2003	$ 3,950,000	$ 3,950,000
Total	$ 9,450,000	$ 9,450,000

TERRITORY AND PLAN OF OPERATION

As of December 31, 2003, the Company was licensed to transact multiple lines of property and casualty insurance in California, Maine, New Mexico, Texas and Vermont. In 2003, the Company wrote $1.95 billion in direct premiums. Of the direct premiums written, $1.9 billion or 97.1% was written in California and $56.4 million or 2.9% was written in the remaining states.

The Company’s insurance business is limited to offering the following types of personal lines property/casualty insurance coverages: private passenger automobile, farm and motor home vehicles, homeowner’s multiple peril, comprehensive personal liability and inland marine.

An applicant, other than an assigned risk, who wishes to be insured by the Company must be a member of the Automobile Club of Southern California (Club) or a subsidiary or affiliated club and must execute a subscriber’s agreement appointing ACSC Management Services, Inc. as attorney-in-fact. The Club is licensed as an insurance broker-agent by the State of California and transacts insurance on behalf of the Company. The Club’s sales agents, approximately 600, are licensed as solicitors and are employed by the Club in this capacity for the Company.

REINSURANCE

Assumed

The Company assumes 100% of the business written by its two Texas subsidiaries, Auto Club Casualty Company and Auto Club Indemnity Company. The Company also assumes 100% of the business written by AAA Texas County Mutual Insurance Company. In 2003, the Company assumed $41.9 million in premiums from these three companies which represents 2.02% of surplus as regards policyholders.

Ceded

The following is a summary of the principal ceded reinsurance treaties inforce as of December 31, 2003:

Type of Contract	Reinsurer (s)	Company's Retention	Reinsurer's Maximum Limit
Homeowner's Property Per Risk Excess of Loss	Platinum Underwriters Reins Inc. (30%), Continental Casualty Company (20%), PMA Capital Insurance Company (20%), Aspen Insurance UK Limited (10%), QBE Reinsurance Corporation (10%), Lloyd's Underwriter Syndicate No 2001 AML (5%) and Transatlantic Reinsurance Company (5%).	$750,000	$2.25 million per risk $4.5 million per occurrence
Homeowners Per Risk Excess of Loss Automatic Facultative	Various Lloyds Syndicates	$3 million	$3 million per occurrence

Type of Contract	Reinsurer (s)	Company's Retention	Reinsurer's Maximum Limit
<u>Property Catastrophe First Layer Excess of Loss – All states except California</u>	Ace Tempest Reinsurance Limited (20%), Axis Specialty Limited (20%), Various Lloyds Syndicate (20%) and Aspen Insurance UK Limited (10%). The Company retains 30%.	$25 million	$50 million per risk
<u>Property Catastrophe Excess of Loss</u>	Various Other Reinsurers (52.51%), Various Lloyds Syndicates (27.49%) and Ace Tempest Reinsurance Limited (15%). The Company retains 5%.	$110 million per occurrence	$240 million per occurrence
<u>Personal Umbrella Quota Share</u>	GE Reinsurance Corporation (12.5%), Hannover Ruckversicherungs Aktiengesellschaft (12.5%), Swiss Re (12.5%), The TOA Reinsurance Company of America (12.5%). The Company retains 50%.	50% of all business	50% of $5 million any one risk

As of December 31, 2003, reinsurance recoverables for all ceded reinsurance totaled $12.1 million or 0.58% of surplus as regards policyholders. Of the ceded reinsurance recoverables, 97.6% were from nonaffiliated authorized reinsurers.

The Exchange's reinsurance agreements are negotiated through a reinsurance intermediary, Guy Carpenter & Company, Inc. and are renewed annually in July.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2003

Underwriting and Investment Exhibit for the Year Ended December 31, 2003

Reconciliation of Surplus as Regards Policyholders
from December 31, 2000 through December 31, 2003

Statement of Financial Condition
as of December 31, 2003

Assets	Ledger and Nonledger Assets	Assets Not Admitted	Net Admitted Assets	Notes
Bonds	$2,416,796,674	$	$2,416,796,674	
Stocks:				
Preferred stocks	33,859,202		33,859,202	
Common stocks	923,658,296		923,658,296	
Real estate:				
Properties occupied by the company	97,585,577		97,585,577	
Cash and short-term investments	137,927,058		137,927,058	
Other invested assets	296,136		296,136	
Receivable for securities	56,382		56,382	
Investment income due and accrued	37,394,939		37,394,939	
Premiums and considerations:				
Uncollected premiums and agents' balances in course of collection	42,664,012	288,407	42,375,605	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	296,105,776		296,105,776	
Reinsurance:				
Amounts recoverable from reinsurers	846,697		846,697	
Current federal and foreign income tax recoverable and interest thereon	5,172,632		5,172,632	
Net deferred tax asset	47,668,000		47,668,000	
Guaranty funds receivable or on deposit	11,257		11,257	
Electronic data processing equipment	25,016,691	20,945,060	4,071,631	
Furniture and equipment, including health care delivery assets	7,844,958	7,844,958	0	
Other assets nonadmitted	500,215	500,215	0	
Aggregate write-ins for other than invested assets	273,523		273,523	
Total assets	$ 4,073,678,025	$ 29,578,640	$ 4,044,099,385	

Liabilities, Surplus and Other Funds			
Losses		$ 626,106,793	(1)
Reinsurance payable on paid loss and loss adjustment expenses		2,791,808	
Loss adjustment expenses		136,073,716	(1)
Other expenses		26,340,099	
Taxes, licenses and fees		6,467,745	
Current federal and foreign income taxes		13,148,519	
Unearned premiums		974,417,612	
Advance premiums		25,730,192	
Dividends declared and unpaid: Policyholders		101,776,000	
Ceded reinsurance premiums payable		452,082	
Amounts withheld or retained by company for account of others		5,512,117	
Provision for reinsurance		54,292	
Payable to parent, subsidiaries and affiliates		6,446,507	
Payable for securities		2,606,055	
Aggregate write-ins for liabilities		42,743,402	
Total liabilities		1,970,666,939	
Unassigned funds (surplus)	$ 2,073,432,446		
Surplus as regards policyholders		2,073,432,446	
Total liabilities, surplus and other funds		$ 4,044,099,385	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2003

Statement of Income

Underwriting Income		
Premiums earned		$ 1,848,423,812
Deductions:		
Losses incurred	$ 1,156,328,650	
Loss expense incurred	184,471,607	
Other underwriting expenses incurred	422,095,899	
Total underwriting deductions		1,762,896,156
Net underwriting gain		85,527,656
Investment Income		
Net investment income earned	$ 120,345,473	
Net realized capital gains	38,412,478	
Net investment gain		158,757,951
Other Income		
Net loss from agents' or premium balances charged off	$ (2,394,104)	
Finance and service charges not included in premiums	47,148,552	
Aggregate write-in for miscellaneous income	4,514	
Total other income		44,758,962
Net income before dividends to policyholders and before federal income taxes		289,044,569
Dividends to policyholders		146,031,101
Federal income taxes incurred		29,500,000
Net income		$ 113,513,468

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2002		$ 1,812,884,147
Net income	$ 113,513,468	
Change in net unrealized capital gains	132,132,288	
Change in net deferred income tax	11,713,000	
Change in nonadmitted assets	2,700,776	
Change in provision for reinsurance	488,767	
Change in surplus as regards policyholders		260,548,299
Surplus as regards policyholders, December 31, 2003		$ 2,073,432,446

<u>Reconciliation of Surplus as Regards Policyholders</u>
<u>from December 31, 2000 through December 31, 2003</u>

Surplus as regards policyholders, December 31, 2000, per Examination			$ 1,780,799,253
	Gain in Surplus	Loss in Surplus	
Net income	$ 203,200,696	$	
Change in net unrealized capital losses		13,124,137	
Change in net deferred income tax	69,972,000		
Change in nonadmitted assets	32,638,926		
Change in provision for reinsurance		54,292	
Totals	$ 305,811,622	$ 13,178,429	
Net increase in surplus as regards policyholders			292,633,193
Surplus as regards policyholders, December 31, 2003, per Examination			$ 2,073,432,446

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

A Casualty Actuary from the California Department of Insurance analyzed the Company's loss and loss adjustment expense reserves. Based on the analysis, the Company's loss and loss adjustment expense reserves as of December 31, 2003, were determined to be reasonably stated and have been accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

There were no recommendations in the current report.

Previous Report of Examination

Accounts and Records (Page 8): It was recommended that the Company provide detail loss and loss adjustment expense reserve work papers upon request. In addition, it was recommended that the Company maintain supporting documentation for all financial statement accounts in sufficient detail as to allow for a full and complete audit trail from the Annual Statement to individual records. The Company has complied with this recommendation.

Loss and Loss Adjustment Expenses (Page13): It was recommended that the Company continue performing regular reviews of its historical data maintained on its computer systems and reevaluate its reserves should the Company find material discrepancies in its data. The Company has complied with this recommendation.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Attorney-in Fact's officers and employees during the course of this examination is hereby acknowledged.

Respectfully submitted,

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Charles DePalma, CFE
Supervising Insurance Examiner
Department of Insurance
State of California